

Consumer and Check Credit

Consider the following procedures at each examination. Examiners are encouraged to exclude items deemed unnecessary. This procedural analysis does not represent every possible action to be taken during an examination. The references are not intended to be all-inclusive and additional guidance may exist. Many of these procedures will address more than one of the Standards and Associated Risks. For the examination process to be successful, examiners must maintain open communication with bank management and discuss relevant concerns as they arise.

- 1 Determine if the bank has offered new consumer loan products since the previous examination and whether management plans to offer additional consumer products in the future.

POLICY CONSIDERATIONS

- 2 Determine whether the institution is engaged in subprime lending in this area or plans to in the future. If subprime lending exists or is planned, consider the subprime lending examination procedures in conjunction with these guidelines. Refer to Subprime Lending Loan Reference module for additional information.

- 3 Determine if policies, procedures, and practices are adequate for the volume and types of consumer credit offered. Determine if consumer loan policies include the following areas (Note: Certain guidelines may be included within separate procedure manuals. Examiners should reference the policies and procedures manuals when performing this review.):

- 3 A Use of credit scoring as an underwriting tool, if applicable.
- 3 B Foreclosure and repossession guidelines.
- 3 C Guidelines for extensions, renewals, modification of terms, deferral of payments, and capitalization of interest.
- 3 D Guidelines for charge-offs (Uniform Interagency Consumer Classification Policy).
- 3 E Guidelines for overdraft lending.
- 3 F Guidelines for handling and tracking problem loans.

ADMINISTRATION

- 4 Determine if internal or external auditors review consumer lending activities. If there is no review or the review is inadequate, assess the workflow procedures, such as underwriting, approving, servicing, and collecting. Proper controls include the following points:

- 4 A Originating officers do not control loan disbursement.
- 4 B Originating officers are not able to independently process payment or alter payment records.
- 4 C Originating officers do not underwrite loans for family members, business associates, of other borrowers that create a conflict of interest.
- 4 D All necessary documents are obtained prior to disbursements.

- 5 Evaluate the system for identifying and reporting consumer loans that warrant the special attention of management.

OPEN-END CREDITS

- 6 Determine whether line overages are permitted per policy and contractual agreement.
- 7 Determine if line overages are monitored, within bank guidelines, and approved.
- 8 Determine if lines that are continually at their maximum usage are periodically reviewed for collectibility.
- 9 Determine if minimum payments are being made by additional draws on the line or other lines of credit within the bank.
- 10 Determine whether credit reports and analyses are updated periodically to ensure that line amounts are appropriate.

INDIRECT LOANS

- 11 Determine if management performs ongoing analysis of each dealer's financial condition and if lines are reaffirmed at least annually.
- 12 Determine if management conducts an independent credit analysis rather than relying on the dealer's credit review.
- 13 Determine if periodic calculations of dealer reserves and holdback agreements are performed.
- 14 Determine how management ensures dealers do not have access to reserve accounts and that proper controls over reserve funding and disbursement are in place.
- 15 Ascertain if customer loan payments are made directly to the bank.
- 16 Verify that the bank controls the title.
- 17 Determine how the bank confirms that dealer selling prices approximate market price.

CONSUMER LEASE FINANCING

- 18 Review the bank's lease accounting for adherence to applicable accounting standards. (Note: Refer to the Direct Lease Financing reference for non-retail activity.)

DOCUMENTATION

GENERAL

- 19 For indirect loans, determine if dealer agreements are adequate and address the following items:
 - 19 A Acceptable types of merchandise.
 - 19 B Credit requirements for borrowers.
 - 19 C Maximum advance and repayment terms.
 - 19 D Discount rate.
 - 19 E Recourse agreement.

19 F Dealer reserve requirements.

20 Determine if the same loan documentation required for direct loans is received on purchased paper.

CREDIT ANALYSIS

21 Review loans prepaid four or more installments. (Such items may represent deficiency balances after application of collateral foreclosure proceeds.)

22 Analyze the level and trend in delinquencies, charge-offs, recoveries, and other key ratios for each type of consumer loan.

23 Analyze the level and trends in the volume of loan renewals or modifications.

24 Determine whether any concentrations exist in loans secured by less liquid or unusual collateral (such as planes and boats).

25 Evaluate management's knowledge of economic trends that influence consumer lending.

INDIRECT LOANS

26 Request and review the following information for each significant dealer:

26 A The dollar amount outstanding.

26 B Delinquencies.

26 C Charge-offs.

26 D Collection reports.

26 E Extensions, deferrals, and renewals.

26 F Report of dealer reserve balances and most recent reserve calculations.

27 Analyze credit quality trends within individual dealer relationships.

28 Review whether dealer limits established are commensurate with the dealer's financial capacity.

29 Determine if management is placing excessive reliance on the dealer's financial capacity rather than the underlying borrower's ability to repay.

30 Review a sample of dealer reserve calculations for reasonableness.

CONSUMER LEASE FINANCING

31 Review lease agreements to determine the types of leases, responsibilities of each party, and collateral protection covenants.

32 Assess the reasonableness of the bank's methodology for estimating collateral residual values.

GENERAL

33 Prepare consumer classifications:

33 A Classify consumer loans in accordance with the Uniform Policy for Classification of Consumer Installment Credit Based on Delinquency Status. (Note: Do not include business installment credits.)

33 B Discuss classifications with management and adjust for justifiable exceptions.